IDAHO OUTLOOK

NEWS OF IDAHO'S ECONOMY AND BUDGET

STATE OF IDAHO **DIVISION OF FINANCIAL MANAGEMENT** **DECEMBER 2007 VOLUME XXX NO. 6**

Even before the books for this year have been closed, economists at Global Insight, Inc. are already thinking about what next year will bring. Their insights for 2008 are especially valuable because the upcoming year will probably be the most challenging year for the economy since the beginning of this decade. Their thoughts have been summarized into their top ten predictions for the economy which are presented below.

One. U.S. economic growth will slow to 1.9% in 2008—its weakest showing over the next few years. The main culprit is housing, which cuts real output by one percentage point. In addition, consumer spending is predicted to slow to 1.7% and business investment will grow a lackluster 2.6%. The only saving grace is net exports, which adds 0.9 percentage points to real GDP in 2008.

Two. Most other regions will also decelerate, as world growth recouples with the slowing U.S. economy. Europe will be hit by the global slowdown, a stronger currency, the continuing credit crunch, housing problems in some countries, and high oil prices. Japan will be similarly afflicted, except for the fallout from the subprime and housing–related problems in the U.S. For Canada and Mexico, weak U.S. growth will be offset by strong oil prices.

Three. The mild global slowdown will only put a small dent in China's rapid growth. Sino credit growth is still very strong and the government's modest tightening efforts have had little impact. After the Beijing Olympics next August, however, the government may have no choice but to tighten credit conditions more dramatically.

Four. Weaker global growth will dampen oil prices and bring them more in line with supply/demand fundamentals. These fundamentals support a price between $75 and $80 per barrel. However, with markets still tight, any type of disruption could send prices back upwards.

Five. Core inflation will edge down. The U.S. economy is operating below its potential, and this will gradually push up the unemployment rate. This extra slack in the economy will put further downward pressure on core inflation. The good news is that energy prices have had little impact on other prices and wage inflation—so far.

Six. The Federal Reserve will keep cutting interest rates. The Central Bank delivered an early Christmas gift by lowering its federal funds rate by 25 basis points on December 11, 2007. It is assumed it will again lower this key rate by 50 basis points in January 2008 and by another 25 points in March. Meanwhile, if the credit crunch and housing problems get worse, the Federal Reserve may have no choice but to inject more liquidity in to the financial system and support the subprime mortgage relief/freeze plan.

Seven. The housing sector will bottom out in mid-2008. Housing will continue to slide in the first half of 2008. During the second half of the year, housing activity is expected to stabilize and begin recovering gradually. The same cannot be said for housing prices, which are likely to keep sliding at least through 2009. The peak-to-trough drop in prices, as measured by the Office of Federal Housing Enterprise Oversight, will be about 10.0%.

Eight. The nation's current-account deficit will continue to improve. The U.S. economy is expected to grow slower than its global counterpart. The dollar has fallen more than 20% in the last five years and should fall a little more. These two developments are supercharging exports and dampening imports. During the course of next year, the positive contribution of trade will prevent the U.S. economy from slipping into a recession.

Nine. The dollar will hit bottom against some currencies in 2008. While the dollar has been sliding since 2002, its recent weakness is a function of fears over the subprime crises and a U.S. recession, combined with expectations of more Federal Reserve cuts. Sentiments for the dollar will begin improving in the second half of 2008 as recession fears ebb. However, both the Japanese yen and Chinese renminbi should continue appreciating against the greenback because of the huge current account deficits the U.S. runs with those countries.

Ten. The economy will be very vulnerable to even a small shock. The combination of the housing/subprime crises and higher oil prices could be enough to push growth into negative territory. If oil prices fall, and end up in the $75-$80 per barrel range early next year, the U.S. economy should skirt a recession. However, either a rise in oil prices or some other shock (even a small one) could cause the economy to retreat.

The Idaho Division of Financial Management wishes everyone a happy and prosperous New Year!

C.L. "BUTCH" OTTER, Governor

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General Fund Update

As of November 30, 2007

	$ Millions		
Revenue Source	FY08 Executive Estimate[3]	DFM Predicted to Date	Actual Accrued to Date
Individual Income Tax	1,392.5	462.0	484.1
Corporate Income Tax	189.1	50.9	50.9
Sales Tax	1,172.2	507.7	516.6
Product Taxes[1]	26.7	12.4	12.5
Miscellaneous	124.8	34.5	38.2
TOTAL GENERAL FUND[2]	**2,905.3**	**1,067.7**	**1,102.2**

1 Product Taxes include beer, wine, liquor, tobacco and cigarette taxes
2 May not total due to rounding
3 Revised Estimate as of August 2007

General Fund revenue was $2.4 million ahead of target in November, making this the fifth consecutive month of revenues above expectations in FY 2008. The total fiscal year-to-date excess stands at $34.6 million. Almost two-thirds of the excess is in the individual income tax category. Approximately one-fourth is in the sales tax category. The two largest months so far this fiscal year have been September and July at $16.7 and $10.7 million above expectations, respectively.

Individual income tax revenue was $2.3 million higher than expected in November. Within the components of the income tax, filing payments were $2.3 million higher than expected for the month. Withholding payments were $1.3 million lower than expected but were offset by refunds that were also $1.3 million lower than expected. The year-to-date excess of $22.1 million from the individual income tax is almost entirely due to filing collections that are ahead by $21.3 million. Withholding collections are up by only $1.2 million for the fiscal year to date and refunds are running $0.7 million higher than expected.

Corporate income tax revenue was $3.2 million higher than expected in November. This brings the fiscal year-to-date shortfall to a mere $0.1 million. The principal reason for November's strength was $3.4 million less in refunds than was expected. For the fiscal year to date, refunds are $7.5 million lower than expected, offsetting $5.6 million less in estimated payments than were expected and $2.0 million less in filing payments.

Sales tax revenue was $2.4 million lower than expected in November, making this the second consecutive month of the fiscal year that sales tax receipts fell short of expectations. However, this is distorted by an accidental overpayment (in the amount of $3.87 million gross, $3.44 million net to the General Fund) that is included in refunds paid in November. Without this distortion November sales tax collections would have actually been $1.0 million higher than expectations for the month. October and November collections related to this mistake have now cancelled out, so the cumulative excess of $8.9 million is accurate.

Product taxes were essentially on target in November. Miscellaneous revenue was $0.5 million below expectations due to light investment earnings.